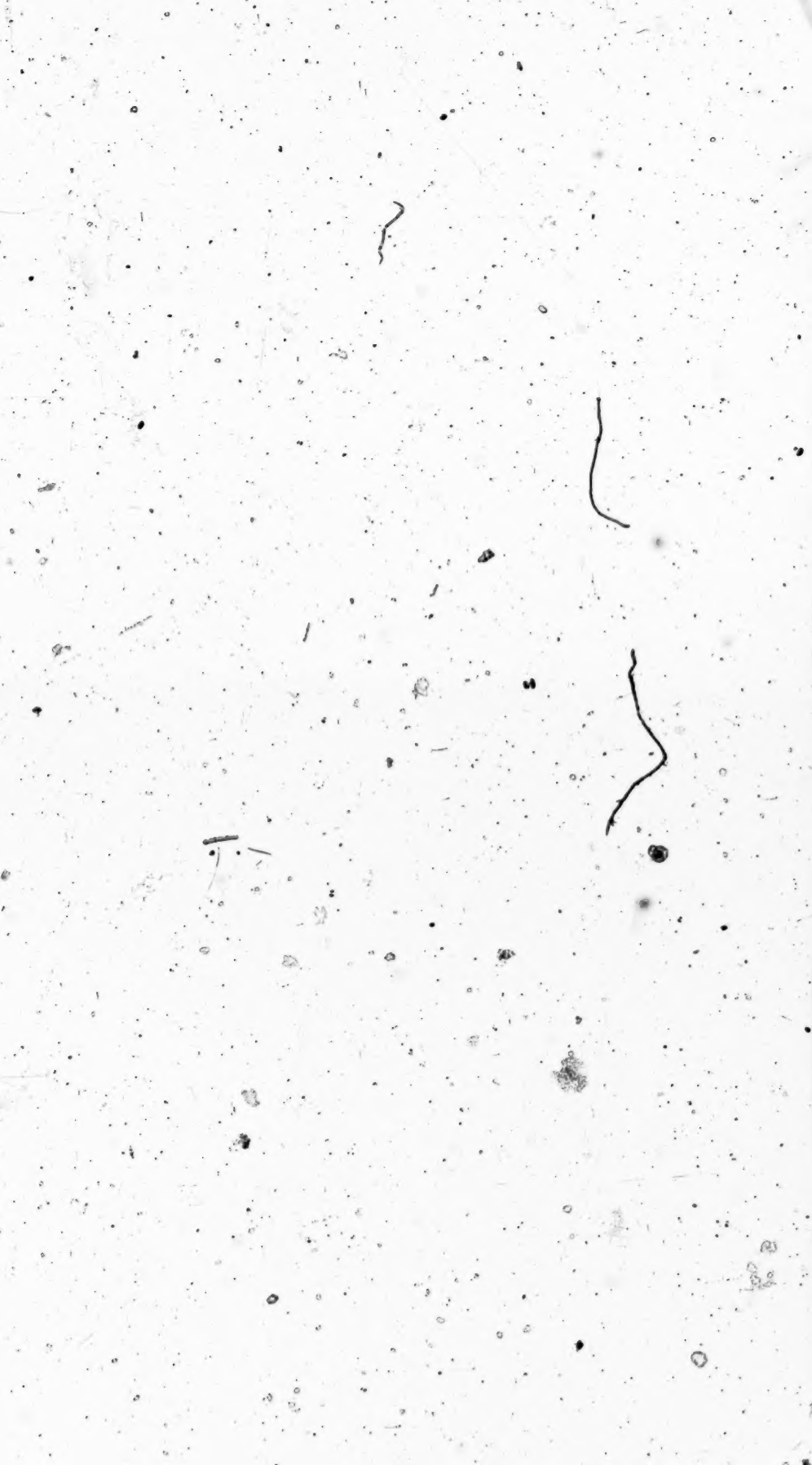

No. 419

In the Supreme Court of the United States

OCTOBER TERM, 1939

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

JOHN KEHOE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONER

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OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 18–32) is reported in 34 B. T. A. 59. The majority and dissenting opinions in the Circuit Court of Appeals (R. 313–322) are reported in 105 F. (2d) 552.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 27, 1939 (R. 322–323). The petition for a writ of certiorari was filed September 27, 1939, and was granted November 6, 1939. The

jurisdiction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below erred in upsetting the finding of the Board of Tax Appeals that there was fraud, malfeasance, and misrepresentation of facts by the taxpayer in entering into a closing agreement, and that such fraud, malfeasance, and misrepresentation of facts materially affected the determination of the taxpayer's income tax liability for 1925, covered by the agreement.

STATUTE INVOLVED

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 1003. (a) The Circuit Court of Appeals and the Court of Appeals of the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board (except as provided in section 239 of the Judicial Code, as amended); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 240 of the Judicial Code, as amended.
>
> (b) Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require. [U. S. C., Title 26, Sec. 641.]

SEC. 1106. * * *

(b) If after a determination and assessment in any case the taxpayer has paid in whole any tax or penalty, or accepted any abatement, credit, or refund based on such determination and assessment, and an agreement is made in writing between the taxpayer and the Commissioner, with the approval of the Secretary, that such determination and assessment shall be final and conclusive, then (except upon a showing of fraud or malfeasance or misrepresentation of fact materially affecting the determination or assessment thus made) (1) the case shall not be reopened or the determination and assessment modified by any officer, employee, or agent of the United States, and (2) no suit, action, or proceeding to annul, modify, or set aside such determination or assessment shall be entertained by any court of the United States.

STATEMENT

The facts, as found by the Board of Tax Appeals (R. 20–25) and as disclosed by the record,[1] may be summarized as follows:

During the taxable year 1925 the taxpayer, John Kehoe, operated a brewery, known as Bartel's

[1] The evidence consists of testimony (R. 50–312) and certain exhibits (R. 41, 312). The exhibits are not set out in the printed record. They were transmitted physically from the Board of Tax Appeals to the court below pursuant to the order of the court below (R. 41, 312) and have been certified to this Court in their original form.

Brewery or McGowan's Brewery, at Edwardsville, Pennsylvania, which was licensed in the name of one P. F. McGowan to manufacture cereal beverages under the National Prohibition Act (R. 20–22, 51, 52, 64–67; Exhibits I, J, K, L). The brewery manufactured legal "near beer," which was sold locally, and illegal "high powered" beer, which was shipped by rail from Kingston, Pennsylvania (R. 21, 24, 86–87, 185–192, 212–213, 227–236; Exhibits FFF, GGG, HHH). Approximately 885 carloads of illegal beer were so shipped in 1925 (a carload consisting of about 100 barrels), and sold at prices ranging from $12 to $17 per barrel (R. 24, 28, 294–295; Exhibits FFF, GGG, HHH; see R. 186–187, 190). Based on the minimum price, the total income derived from the illegal sales (after deducting $98,648.60 freight paid) was at least $890,000 (R. 24, 28). The brewery was operated by the taxpayer through an arrangement with McGowan from February 1924 until February 28, 1927 (R. 21, 86, 90, 91–92, 106–107, 165–166).

McGowan was employed by the taxpayer in February 1924, to act as lessee of the brewery and to secure permits for its operation (R. 20–22, 51, 63–65, 104–106). He was advised by the taxpayer to follow the instructions given by William F. McHugh, manager of the brewery, who would in turn receive his instructions from the taxpayer (R. 20, 23, 51–52, 236–237). He signed thereafter such leases, applications for permits,

and contracts as he was requested to sign by the taxpayer or by McHugh (R. 20–23, 63–65, 72–73, 76–79, 80–81, 160–162). He performed no regular services (R. 22, 84, 216). He was told by the taxpayer to "keep [his] mouth shut" concerning the brewery and at times was sent on trips, at the expense of the taxpayer, to get him away from the brewery (R. 20–23, 83–86, 101, 106, 170–171). The taxpayer paid McGowan $150 per month at first and $200 per month after the first permit was issued, and from time to time gave him additional amounts (R. 23, 81–84, 169–171).

In connection with the original permit and the renewal permits obtained in the name of McGowan, the taxpayer and his brother, Tom Kehoe, executed an indemnity agreement and later a joint note in the amount of $25,000 for the protection of a surety company which issued the indemnity bond required by the Prohibition Administration (R. 21–22, 193–195, 198–200, 177–178, 279–280, 283–285, 287; Exhibits P, VV, TTT). McGowan opened one bank account with funds supplied by the taxpayer (R. 20, 63). Another was opened in McGowan's name but without his knowledge by someone else, and checks were drawn upon it by Charles J. Locke, the bookkeeper of the brewery, and signed by McHugh (R. 23, 113–116, 121–123, 124–126). McGowan had no financial interest in the brewery (R. 22, 81). The real party in interest was the taxpayer (R. 22).

The regular books of the brewery, which were kept by Charles J. Locke, did not not show charges for freight on the illegal beer or receipts from sales of such beer (R. 23, 212–213, 216–217, 219; Exhibits BBB, CCC, DDD, EEE). Records of these transactions were kept in another set of books in the back office of the brewery (R. 24, 213–214). From the records relating to the "near beer" business, Locke prepared income-tax returns for McGowan for the years 1924, 1925, and 1926, in which he purported to return the income from the brewery (R. 23–24, 110–111, 121–122, 212–213). The return for 1925 showed a net loss of $82,325.97 (R. 24; Exhibit FF). No amounts were included in these returns to reflect the sales of illegal "high powered" beer (R. 24, 121–122, 212–213).

The taxpayer reported no income from the brewery or from the sale of any beer in his 1925 income-tax return filed March 15, 1926 (R. 24; Exhibit LLL). This return, which was signed by him and purported to be a joint return of himself and his wife,[2] disclosed a net income of $19,198.33 and a tax liability of $194.56 (R. 5–6, 10–11, 15, 20, 24; Exhibit LLL). It did not state the nature of the taxpayer's business or occupation (Exhibit LLL). His return was prepared by his secretary from data shown by his books (R. 254–256).

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[2] She was a party to the petition for a redetermination of the deficiency, and the Board decided that as to her there was no deficiency (R. 4–9, 31).

After an investigation the Commissioner, on October 20, 1927, sent to the taxpayer and his wife a notice of a deficiency in the amount of $9,563.86 (R. 6, 10–11, 24–25). The nature of the additional income of $53,990.46 on which this deficiency was based is not disclosed by the record (R. 5–6, 10–11, 317). This deficiency was assessed and paid November 15, 1927 (R. 6, 10–11, 24). Thereafter an agreement in writing was entered into between the taxpayer and the Commissioner fixing the total liability for tax and interest for the year 1925 at $10,631.74, which represented the tax originally paid, the deficiency of $9,563.86, and the interest due (R. 6, 10–11, 24–25). This agreement was approved by the Acting Secretary of the Treasury on January 27, 1928 (R. 6–7, 11, 25).

In June 1929 the Commissioner was informed of the operation of what was known as Bartel's or McGowan's Brewery, and that John Kehoe was the owner of the brewery during 1925 (R. 25, 108–109; Exhibit 1). The informers were McGowan, Paul T. Jones, and George N. Murdock, who in March 1932 filed a claim for a reward for having given the "first information" which led to the detection of John Kehoe for violation of internal revenue laws (R. 108–109, 135–144, 250–252; Exhibit 1). The nature of the information given by the informers is indicated by Exhibit 1.

On January 3, 1930, the Commissioner notified the taxpayer in writing that it was necessary to

make a further examination of his income-tax liability for 1925 (R. 25, 305–306; Exhibit CCCCC). On February 13, 1932,[3] the Acting Secretary of the Treasury approved a cancelation and revocation of the closing agreement and directed the Commissioner to take such further action to adjust the tax liability for the year 1925 as might be in order (R. 25, 306–307; Exhibit DDDDD). On February 24, 1932, the Commissioner mailed a deficiency notice to the taxpayer and his wife, asserting a deficiency of $208,043.36 and a fraud penalty of $108,803.61 (R. 4, 8–9, 10, 19, 25). The deficiency was based on income of $890,000 from the brewery which had not been reported (R. 9, 29).

Besides finding these facts, the Board in its opinion concluded that "large amounts of income were received in cash by or for the [taxpayer] from the operation of the brewery in 1925, and that the receipt of this income has never been reported nor disclosed by him" (R. 28). It also pointed out that the taxpayer "has at all times denied and still denies any connection whatever with its operation" (R. 26, 28). The denials are made in his pleadings before the Board (R. 15–16), in which the taxpayer and his wife "deny that petitioner John Kehoe derived any income from that source [the operation of the brewery] during the calendar year 1925" (R. 15) and in addition "deny that petitioner John Kehoe derived income in the year 1925 from the

[3] The Board's finding (R. 25) erroneously gives the date as February 13, 1933, but see R. 306; Exhibit DDDDD.

operation of the P. F. McGowan Brewery of Edwardsville, Pennsylvania, either in the amount of $890,000.00 or in any other amount" (R. 16). The pleadings also show that Kehoe was indicted for income-tax evasion on March 4, 1932, and that the indictment was subsequently dismissed because it had not been returned within three years after the commission of the offense charged (R. 7, 13–14, 15).

On the basis of the evidence before it, the Board found that the 1925 return was false and fraudulent, with intent to evade the tax; that the deficiency here involved was due to fraud with intent to evade the tax; and that there was misrepresentation by the taxpayer of material facts affecting the determination and assessment covered by the closing agreement (R. 25, 28–29). The Board in its opinion also adverted to the evidence clearly indicating the receipt by the taxpayer of amounts much greater than those upon which the deficiency was computed (R. 30) and, since no deductions were proved by the taxpayer, sustained the deficiency determined against the taxpayer by the Commissioner (R. 29–30, 32). It likewise sustained the penalty determined by the Commissioner (R. 30, 32). It found that Mrs. Kehoe realized no income from the brewery, and was not guilty of fraud affecting the 1925 tax, and determined that the deficiency and fraud penalty should be assessed against Kehoe alone (R. 25, 31, 32).

The court below held that the Board was warranted in finding that Kehoe illegally operated the

brewery, concealing his identity, and that during the taxable year 1925 he realized income amounting to over $890,000 from that source, but held that the Commissioner had not sustained the burden of proving that the closing agreement was entered into through fraud, malfeasance, or misrepresentation, and reversed the Board (R. 313–318, 323).

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In failing to hold that the Board's finding that there was fraud, malfeasance, and misrepresentation by the taxpayer of material facts affecting the determination of the deficiency covered by the 1927 closing agreement was supported by substantial evidence.

2. In usurping the power of the Board by weighing the evidence and drawing its own inference from the facts and substituting its inference for the Board's ultimate finding of fact.

3. In holding that fraud, malfeasance, and misrepresentation by the taxpayer in the execution of the closing agreement could not be proved except by direct testimony that no income from the brewery was included in the additional income on which the deficiency covered by the closing agreement was based.

4. In holding that because there was no direct testimony as to whether or not any brewery income was included in computing the deficiency on which the 1927 closing agreement was based, the

Board was obliged to draw the inference that such income was included and that there was no fraud, malfeasance, or misrepresentation in the closing agreement.

5. In disregarding evidence establishing continuous actual concealment by the taxpayer of his connection with the brewery until after the closing agreement was signed.

6. In disregarding evidence establishing that the Government did not know of Kehoe's connection with the brewery until McGowan's disclosures in 1929.

7. In reversing a finding of fact of the Board where it does not appear that the evidence, with every reasonable inference that may be drawn therefrom in the petitioner's favor, is insufficient to sustain it.

8. In reversing the Board's order redetermining a deficiency of $208,043.36 and a fraud penalty of $108,803.61.

ARGUMENT

THE COURT BELOW ERRED IN UPSETTING THE FINDING OF THE BOARD THAT THERE WAS FRAUD, MALFEASANCE, AND MISREPRESENTATION OF FACTS BY THE TAXPAYER IN ENTERING INTO A CLOSING AGREEMENT WHICH MATERIALLY AFFECTED THE DETERMINATION OF HIS INCOME-TAX LIABILITY FOR 1925, COVERED BY THE AGREEMENT

This case turns simply upon a question of fact: Whether there was fraud or malfeasance or misrepresentation of fact materially affecting the de-

termination or assessment of the tax covered by the 1927 closing agreement (Section 1106 (b), *supra*, p. 3).[4]

In entering into a closing agreement, the taxpayer has a duty to disclose fairly and honestly his entire income from all sources. A closing agreement is authorized by Section 1106 (b) only after a determination and assessment has been settled by the payment in full of any tax found to be due. The agreement is the culmination of negotiations between the taxpayer and his Government and at some time during those negotiations the Government is entitled to have from the taxpayer a full statement of his income producing operations. If he has fully disclosed them on his return, there is no additional duty to disclose them again. But where, as here, there has been no prior disclosure, the Government is entitled to the facts before the agreement is signed. The taxpayer does not deny that such a duty rested on him. He merely contends that the Government failed to prove that it had no such knowledge at the time of the closing agreement in question.

1. THE BOARD OF TAX APPEALS MADE FINDINGS OF FACT WHICH, IF SUPPORTED BY SUBSTANTIAL EVIDENCE, WERE CONCLUSIVE ON THE COURT BELOW.

The pleadings of the parties before the Board of Tax Appeals raised the issue whether there was

[4] The finding of the Board (R. 25-26, 28) that the 1925 return was false and fraudulent with intent to evade tax and that the deficiency here involved could be assessed at any time under Section 278 (a), does not appear to be challenged.

fraud or malfeasance or misrepresentation of fact materially affecting the determination of the tax covered by the 1927 closing agreement.[5] The Board on the evidence adduced before it decided this issue against the taxpayer. Specifically, the Board found as a fact (R. 25) that the taxpayer's 1925 return was false and fraudulent, with intent to evade tax; that the deficiency here involved was due to fraud with intent to evade tax; and that there was misrepresentation by the taxpayer of material facts affecting the determination and assessment covered by the closing agreement. These conclusions of fact were more fully stated by the Board in its opinion as follows (R. 29):[6]

> We further hold that the facts disclosed definitely show fraud, malfeasance, and mis-

[5] The taxpayer, in his appeal to the Board, raised, among other questions, the issue whether the Commissioner, with the approval of the Secretary of the Treasury, was justified in setting aside the closing agreement executed on December 27, 1927, and January 25, 1928 (R. 5, 8). The Commissioner in his answer alleged that the taxpayer had withheld information concerning the operation of the brewery and that the agreement had been revoked because induced by fraud, deceit, malfeasance, and misrepresentation of facts materially affecting the subject matter of the agreement (R. 10–14). The taxpayer first specifically denied these allegations in his reply (R. 15) and then further denied that he had received income from the operation of the brewery "either in the amount of $890,000 or in any other amount" (R. 16).

[6] Conclusions of fact appearing in the course of the Board's "opinion" have the full force and effect of findings of fact. *Flynn* v. *Commissioner*, 77 F. (2d) 180 (C. C. A.

representation of facts materially affecting the determination and assessment of the tax covered by the final closing agreement and that the respondent, acting with the approval of the Secretary of the Treasury, was justified in going behind the said closing agreement in making the determination which forms the basis of this proceeding. * * * We have found that the petitioner, with intent to evade tax, failed to report in his return income received from the operation of the brewery and on the record it is apparent that he made no disclosure of such income at the time of executing the closing agreement, nor at any other time. While the filing of a return and the signing of a closing agreement are separate and distinct and fraud in one does not necessarily indicate fraud in the other, the same or a continuing act, that of wilfully concealing income, may be, and on the facts of this case, is a sufficient basis for finding that the return was fraudulent with intent to evade tax and further that there was a misrepresentation of a material fact in the execution of the closing agreement.

It is settled that "Fraud is always a question of fact to be determined by the court or jury upon a

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5th); *Keck Inv. Co.* v. *Commissioner*, 77 F. (2d) 244 (C. C. A. 9th), certiorari denied, 296 U. S. 633; *Insurance & Title Guarantee Co.* v. *Commissioner*, 36 F. (2d) 842 (C. C. A. 2d), certiorari denied, 281 U. S. 748; *Olson* v. *Commissioner*, 67 F. (2d) 726 (C. C. A. 7th), certiorari denied, 292 U. S. 637.

careful scrutiny of the evidence before it." *Smith* v. *Vodges, Assignee,* 92 U. S. 183, 184; also *Laidlaw* v. *Organ,* 2 Wheat. 178, 194; *Warner* v. *Norton,* 20 How. 448, 460; *Ball* v. *Warrington,* 108 Fed. 472, 475 (C. C. A. 3d). The trier of the facts likewise determines the issue whether assets have been fraudulently concealed. *Dean* v. *United States,* 51 F. (2d) 481, 483 (C. C. A. 9th); *Kern* v. *United States,* 169 Fed. 617 (C. C. A. 6th). Compare *Tyler* v. *Savage,* 143 U. S. 79, 98; *Stewart* v. *Wyoming Ranche Co.,* 128 U. S. 383. The existence of fraud, concealment, or bad faith is peculiarly within the province of the trier of the facts to determine. It is often ascertainable only from a great variety of circumstances, none of which is conclusive. See *Mammoth Oil Co.* v. *United States,* 275 U. S. 13, 36; *Wood* v. *United States,* 16 Pet. 342, 360–361; *Castle* v. *Bullard,* 23 How. 172, 187. Such findings of fact have been declared by this Court to be binding on appeal. *Clark* v. *United States,* 131 U. S. (Appendix LXXXV, LXXXVI), 18 L. Ed. 915. We submit that these settled principles are at least equally applicable to findings of fraud and misrepresentation by the Board (Section 1003 (b), *supra,* p. 2). *Mitchell* v. *Commissioner,* 89 F. (2d) 873, 874–875 (C. C. A. 2d), reversed on other grounds, 303 U. S. 391; *Wickham* v. *Commissioner,* 65 F. (2d) 527, 529, 532 (C. C. A. 8th); *Commissioner* v. *Hales,* 76 F. (2d) 916 (C. C. A. 7th). Compare *Helvering* v. *National Grocery Co.,* 304 U. S. 282,

294. The sole issue within the competence of the court below to determine, therefore, was whether there was any substantial evidence to support the findings and decision of the Board. See *Helvering* v. *Lazarus & Co.*, No. 56, this Term; *Elmhurst Cemetery Co.* v. *Commissioner*, 300 U. S. 37, 40.

2. THE EVIDENCE AMPLY SUPPORTS THE FINDINGS OF FACT OF THE BOARD OF TAX APPEALS

The court below (composed of Judges Davis and Buffington, with Judge Biggs dissenting) upset the Board's findings of fact and held that the Commissioner had not sustained the burden of proving that the closing agreement was entered into through fraud or malfeasance or misrepresentation of fact (R. 493–498). In so doing the court ignored substantial evidence in the record and usurped the jurisdiction given to the Board by weighing the evidence and substituting its own findings for those of the Board. Section 1003 (b), *supra*, p. 2; *Helvering* v. *Lazarus & Co.*, No. 56, this Term; *Palmer* v. *Commissioner*, 302 U. S. 63; *Elmhurst Cemetery Co.* v. *Commissioner*, 300 U. S. 37.

The evidence adduced in this case amply supports the findings of fact made by the Board. We need not review all the evidence in detail. The following constitutes substantial evidence of Kehoe's continuous actual concealment from the Bureau of Internal Revenue of his brewery income for the year 1925, from the time the 1925 return

was filed until long after the 1927 closing agreement was executed:

1. John Kehoe at the time his 1925 return was filed (on March 15, 1926) concealed his connection with the brewery (R. 24, 28–29; Exhibit LLL). He did not report income in any amount from that source or from the sale of beer and failed to fill in the blank stating the nature of his business (R. 24, 28–29, 110–111, 121–122, 212–213; Exhibit LLL).[7] His income was reported as derived from real-estate operations, dividends, interest, and election bets (Exhibit LLL). This return, as found by the Board, was false and fraudulent with intent to evade tax (R. 25, 28).[8]

2. The brewery was operated by Kehoe, the real party in interest, in the name of his employee, McGowan, from February 1924 to February 28, 1927 (R. 20–23, 51, 52, 63–66, 81–82, 86, 90, 91–92, 105–107, 165–166). McGowan, acting under instructions from Kehoe, posed as ostensible proprietor: he entered into contracts as lessee, secured permits to operate in his own name, and as owner filed returns purporting to reflect the income from

[7] He likewise failed to answer this question in his 1924 return (Exhibit KKK) and in his 1926 return (Exhibit MMM), although he stated in his 1923 return that his business was "real estate and electrical business" (Exhibit JJJ).

[8] The fact that the return was prepared by his secretary from information furnished by Kehoe (R. 254–256) does not relieve him of the fraud, for he executed the return and took oath to its truthfulness (R. 5, 10, 15, 24); *Cooper* v. *United States*, 9 F. (2d) 216 (C. C. A. 8th).

the operation of the brewery (R. 22–23, 64–66, 76–77, 110–111, 121–122, 212–213).

3. The illegal operations of the brewery and Kehoe's interest in them were kept strictly secret (R. 22–24, 101, 106, 128–132, 153, 160–161, 213–214). Charles Locke, the regular bookkeeper, never saw the records of the illegal operations and never went into the brewery when "high powered" beer was being made (R. 23–24, 212–214, 221, 223–224). Even the weekly bonus paid to the employees was always distributed in cash and was not recorded in the regular books (R. 220–221). Kehoe refused to accept a check from Harry Kenny, who bought beer from him, and insisted on being paid in cash (R. 186–187). Kehoe at times used the alias "W. J. Vincent" when endorsing checks (R. 262–263; Exhibit RRR). When there was "trouble" at the brewery, Kehoe sent the ostensible owner, McGowan, away in a new roadster (R. 83–84). McGowan made several similar trips under instructions from Kehoe and at the latter's expense (R. 84–85, 169–171). On some of these occasions McGowan was followed by revenue agents (R. 170).

4. Kehoe took elaborate precautions against any disclosure of his connection with the brewery (R. 22–24, 81–85, 101, 106, 131–132).[7] McGowan saw

[7] Kehoe, under date of May 26, 1924, wrote to his Congressman at Washington, D. C., expressing vital interest in the permit to be issued. He stated: "Treat this matter strictly confidential so far as I am concerned * * *" (Exhibit OOO).

Kehoe at the brewery only once during the three years of operation but held meetings with him and McHugh as frequently as three times a week at his office in Pittston, Pennsylvania, several miles away (R. 100–101, see 226–227). Kehoe instructed McGowan to talk to no one concerning the brewery and to assert, if questioned by one James McQuade, that his cousin, Con Dorian, was interested in the brewery and that the taxpayer had no connection with it (R. 101, 104–105, 106). On January 25, 1927, Kehoe urged McGowan to swear falsely that the latter was sole owner of the brewery in order that Kehoe might use the statement to answer his political enemies (R. 162; Exhibit 2). McGowan signed the false statement as requested (R. 153, 160–161, 161–163; Exhibit 2).

5. Kehoe planned to continue to operate the brewery during the year 1927 (R. 22, 90–92, 106–107). In the early part of 1927, when the brewery was about to lose its permit, Kehoe sought to obtain a new permit to operate during that year in the name of one John Carroll (R. 22, 90–92, 106–107). McGowan was paid $500 and ordered to turn the plant over to Carroll (R. 90–91). When that plan failed, McGowan, in late February 1927, was instructed to hand over the beer to the National Prohibition Department, and did so in his own name (R. 90–91, 106–107).

6. Kehoe, concerned lest his interest in the brewery be disclosed, on occasion promised to reward McGowan with substantial amounts of money in

order to ensure his continued silence (R. 22–23, 82–84, 129–132, 138–139). Thus, when "trouble" arose in Cleveland, Kehoe agreed to pay McGowan $60,000 to $75,000 in the event McGowan had to take "the rap" (R. 129–131). Kehoe made a similar promise in April, 1928 (R. 138–139). On the Friday before April 19, 1928, when the court below decided *United States* v. *Glass*, 25 F. (2d) 941, holding that McGowan, McHugh, and others could not be removed to the Northern District of Ohio to stand trial on an indictment charging them with conspiracy to violate the National Prohibition Act,[10] McGowan was told by Kehoe that if he was returned to Cleveland he must go to jail but that Kehoe would pay him $60,000 to $70,000 (R. 102–103, 138–139).

7. Kehoe was not indicted with McGowan and McHugh.[11]

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[10] McGowan was indicted and arrested in June 1927, but was released on bail provided by a surety company. He did not put up any collateral with the surety company nor pay any premium on the bond, nor did he employ or pay the attorney who appeared at the time of his release. Upon his release, he went with the attorney to the office of Kehoe in Pittston (R. 92–95). McGowan likewise did not employ any of the attorneys who represented him in the court below in the case decided April 19, 1928 (R. 102–103).

[11] When the court below on April 19, 1928, decided the case of *United States* v. *Glass*, 25 F. (2d) 941, involving a conspiracy in connection with the unlawful operation of the brewery, Kehoe's real interest still seems to have been concealed and undisclosed. It may be noted that the indictment there involved refers to payments by check made to one W. J. Vincent, a party not indicted and apparently un-

8. McGowan's break with Kehoe occurred after Kehoe refused to pay him and after the court below handed down its decision of April 19, 1928 (R. 138–139). McGowan and his associates did not inform the Government of Kehoe's activities until June, 1929 (R. 24–25, 108–109, 138–139; Exhibit 1).

9. McGowan and his associates filed a claim in 1932 for having given the first information [12] leading to the determination of the deficiency here involved (R. 139–144, 250–251; Exhibit 1).

10. In his reply to the Commissioner's answer in this case, Kehoe still denied all connection with the brewery,[13] and the principal issue before the Board

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known (25 F. (2d) at 944). W. J. Vincent was an alias sometimes used by Kehoe in endorsing checks (R. 262–263; Exhibit RRR).

[12] The fact that the words "first information" appear on the printed form on which the claim was filed in no way detracts from the significance of this evidence (see Br. in Opp. 3–4, 13). The claim is in fact one for having given *the first information.*

[13] This denial in the taxpayer's pleadings does not lose any of its significance on the ground that it might—but properly should not—be viewed as being addressed to another issue in the case, i. e., the issue whether the original return was false (see Br. in Opp. 16–17). In paragraph 5 (g) of the reply (R. 15) the taxpayer, meeting paragraph 5 (g) of the answer (R. 12), categorically denied that he derived any income from the brewery in 1925. Just before concluding his reply, Kehoe also denied, generally and unqualifiedly, that he derived income from the brewery in 1925, "either in the amount of $890,000.00 or in any other amount" (R. 16). A party is bound by his pleadings, and statements made therein must be assumed against him as judicial admissions. See *Darling Shops of Tennessee v. Brack*, 95 F. (2d) 135, 141 (C. C. A. 8th), and cases there cited. It may be observed

was whether or not he was its owner and operator (R. 14–16, 26, 28). The examination of witnesses by Kehoe's counsel throughout the hearing before the Board in 1934 clearly indicated that his connection with the brewery was vigorously contested even then (see R. 26, 28), and led the Board to observe that "It is strenuously argued that the respondent has failed to show any connection between petitioner John Kehoe and the operation of the brewery business, except through the testimony of Patrick F. McGowan, whose credibility is seriously questioned" (R. 26). The Government called Kehoe to the stand to testify to his signature upon the indemnity agreement executed by himself and his brother with the American Surety Company (R. 179–185). Kehoe examined his signature but refused to swear either that it was or was not his own (R. 179–185; see R. 261–273). The evasive character of Kehoe's testimony and his reluctance to concede his execution of the instrument (showing his connection with the brewery) is evident on the record.

11. The additional income on which the deficiency covered by the closing agreement was based was about $53,000, whereas the income derived from illegal operations of the brewery was $890,000 (R. 5, 10, 13, 15, 24, 28).[14] McGowan in his 1925

that since in 1932 the taxpayer denied he had received income from the brewery *in any amount*, the inference is clear that he must not have disclosed, nor paid a tax on, any such income in 1927.

[14] In computing the income on which the deficiency here involved is based, the Commissioner in his letter (R. 8–9)

income-tax return had reported a loss on its legal operations (R. 23–24, 110–111, 121–122, 212–213; Exhibit FF).

The inferences fairly to be drawn from such evidence are a matter of common sense and need not be spelled out at length. Here there was overwhelming proof that Kehoe sought to conceal his interest in the brewery, not only from the Government, but from the general public, during the entire period from 1925 until 1934: He attempted to defraud the Government by filing (in March 1926) a false income-tax return for the year 1925. He compelled McGowan to perjure himself in January 1927. He promised McGowan a huge sum in April 1928; plainly this was to ensure his continued silence. He denied receiving income in any amount from the brewery in his pleadings filed in 1932. He contested bitterly during the trial in 1934 every piece of evidence tending to establish his connection with the brewery. When the Government called him as witness he refused even to admit his own signature on the indemnity agreement executed

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did not charge the taxpayer with the income of $53,990.46 on which the additional tax had been paid in 1927, although in computing the tax due he gave him credit for the amount of the additional tax then paid, $9,563.86. The failure to add that income in the computation is undoubtedly due to a mere oversight, but, however caused, it is an error in the taxpayer's favor. It does not mean, as has been claimed by the taxpayer (Br. in Opp. 4–5, 13–14), that the $53,000 was embraced in the $890,000 income from the brewery which the letter stated had not been reported, and does not lend support to the argument that the $53,000 was income from the brewery.

with the American Surety Company. The conclusion is irresistible that Kehoe never disclosed any information to the Government about his connection with the brewery, either at the time of the closing agreement in 1927 or at any other time. Compare *N. Y. Mut. Life Ins. Co.* v. *Armstrong*, 117 U. S. 591, 598; *Commissioner* v. *Dyer*, 74 F. (2d) 685, 686 (C. C. A. 2d), certiorari denied, 296 U. S. 586; *Engler* v. *United States*, 25 F. (2d) 37, 39 (C. C. A. 8th).

The majority of the court below assumed (R. 317) that the only manner in which the Commissioner could prove fraud, malfeasance or misrepresentation was by direct testimony that no income from the brewery was included in computing the deficiency on which the closing agreement was based. There was no justification for such an assumption. It is settled that fraud can be established by circumstantial evidence (*Mammoth Oil Co.* v. *United States*, 275 U. S. 13, 36; *Wood* v. *United States*, 16 Pet. 342; *Castle* v. *Bullard*, 23 How. 172, 187), and that concealment constitutes fraud or misrepresentation when one is under a duty to speak (*Stewart* v. *Wyoming Ranche Co.*, 128 U. S. 383; *Tyler* v. *Savage*, 143 U. S. 79, 98).

The argument is advanced by Kehoe in slightly altered form (see Brief in Opposition, pp. 2, 8, 12–18, 20). He urges that the failure to introduce direct testimony as to the income covered by the closing agreement precluded the Board from finding that the income from the brewery was not so

covered. This is plainly a *non sequitur*. The evidence that was introduced established that Kehoe himself never disclosed to the Government the receipt of any income from the brewery. There was no basis in the record for concluding that the Government had obtained such information from any other source until after the execution of the 1927 closing agreement. The elaborate precautions taken by Kehoe to conceal his interest in the brewery militated against an assumption that the Bureau had discovered the fraud through its investigation in the summer of 1927. A claim for having given (in June 1929) the *first information* that the 1925 return was fraudulent was filed by McGowan and his associates with the Bureau in 1932. In addition, the persistent manner in which Kehoe during the trial contested his connection with the brewery was inconsistent with a claim that an accord had been reached between him and the Bureau on that issue in 1927. Kehoe's continued concealment was very substantial evidence of his fraud. See *N. Y. Mutual Life Ins. Co.* v. *Armstrong*, 117 U. S. 591, 598; *Commissioner* v. *Dyer*, 74 F. (2d) 685, 686 (C. C. A. 2d), certiorari denied, 296 U. S. 586; *Engler* v. *United States*, 25 F. (2d) 37, 39 (C. C. A. 8th). The Government clearly produced evidence that would support a finding that the determination covered by the 1927 closing agreement was materially affected by fraud and misrepresentation of facts on the part of Kehoe. Yet despite this evidence tending to estab-

lish that the closing agreement was invalid, Kehoe rested his case. He did not introduce the 1927 closing agreement itself into evidence. He did not take the stand to testify that the income from the brewery had been included in the agreement. The inference is plain: the 1927 closing agreement did not show on its face that income from the brewery was covered by it and Kehoe could not have so testified. See *Mammoth Oil Co.* v. *United States*, 275 U. S. 13, 52–53. On this record, surely, there can be no doubt that the Board was justified in its finding; first, that "the petitioner [Kehoe], with intent to evade tax, failed to report in his return income received from the operation of the brewery and on the record it is apparent that he made no disclosure of such income at the time of executing the closing agreement, nor at any other time" (R. 29), and second, that Kehoe's willful and continuing concealment of his income from the brewery constituted both "a sufficient basis for finding that the return was fraudulent with intent to evade tax and further that there was a misrepresentation of a material fact in the execution of the closing agreement" (R. 29). It follows that the Board correctly held that the closing agreement did not bar the determination, assessment, and collection of the tax and penalty lawfully due from Kehoe for the year 1925.[6]

[6] Kehoe cannot now challenge the amount of the deficiency. He elected to stand on the fraud issue alone (R. 30) and failed to introduce any evidence to establish his

The result would be the same, moreover, even if the record did not refute the assumption, made by the majority of the court below, that income from the brewery was included in the additional income of $53,990.46 upon which the assessment covered by the closing agreement was based. As Judge Biggs, in his dissenting opinion, points out—

> even if such assessment was shown to have included income acquired by the petitioner [Kehoe] from the illegal operation of the brewery, there is no evidence showing that the whole or any substantial part of the income of the petitioner from his illegal operations was included in the assessment or covered by the closing agreement. Seemingly the petitioner [Kehoe] takes the position that if he disclosed any portion of his illegal income to the United States in 1927 or if he was assessed by the United States upon any portion of that illegal income in that year, he may claim the protection of the closing agreement. The success of such a contention would place a great premium upon fraud (R. 321).

The position so well stated by Judge Biggs is, in our opinion, entirely sound and well supported by the record. It is manifest on this record that the *net income* Kehoe received from the operation

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right to any deduction from the income he was shown to have received. See *Helvering* v. *Taylor*, 293 U. S. 507, 514; *New Colonial Co.* v. *Helvering*, 292 U. S. 435. The evidence establishes the receipt by Kehoe of taxable income in excess of the amount ($890,000) used as the basis for computing the deficiency here involved (R. 9, 28, 30).

of the brewery was many times the amount covered by the closing agreement.[16]

3. THE COURT BELOW USURPED THE JURISDICTION OF THE BOARD OF TAX APPEALS

The suggestion in the opinion of the majority of the court below (R. 316) that the Board's findings in fraud cases do not have the same weight as in other cases is wholly unsupported. It is true that the burden of proof in such cases is upon the Commissioner. But that fact in no way affects the conclusiveness of the Board's findings of fact where, as here, they are supported by substantial evidence. *Mitchell* v. *Commissioner*, 89 F. (2d) 873 (C. C. A. 2d), reversed on other grounds, 303

[16] Kehoe's *gross receipts* from the illegal operations of the brewery were between $1,062,000 (figured at $12 per barrel sold) and $1,504,500 (figured at $17 per barrel) (R. 28). His *expenses* for freight aggregated $98,648.60 (R. 28). There is clear evidence that the other *expenses*, such as materials and labor, with minor exceptions, were charged against the legal operations of the "near" beer business. Thus, the legal operations were charged with expenses of over $180,000 on a gross business of only $97,713.19 (R. 24; Exhibit FF). McHugh's salary and that of the other employees (with the exception of an $8-per-week cash bonus) was charged against "near" beer operations (R. 216, 221). The inventory account on the "near" beer books included beer that had not been dealcoholized (R. 43, 218). The rent of $52,399.92 paid in 1925 was charged entirely against the legal operations (see R. 20; Exhibits FF, CCC, EEE). Plainly, the major portion of the cost of acquiring the illegal receipts was included in the expenses charged against the legal operations on the "near" beer books and taken as a deduction in the 1925 return filed by McGowan, acting as agent for Kehoe.

U. S. 391; *Wickham* v. *Commissioner*, 65 F. (2d) 527 (C. C. A. 8th); *Commissioner* v. *Hales*, 76 F. (2d) 916 (C. C. A. 7th); *Goldberg* v. *Commissioner*, 100 F. (2d) 601 (C. C. A. 7th), certiorari denied, 307 U. S. 622; *Schallman and Geller* v. *Commissioner*, 102 F. (2d) 1013 (C. C. A. 6th). See also *Commissioner* v. *Ingram*, 87 F. (2d) 915 (C. C. A. 3d).

It was the function of the Board to weigh the evidence, to draw the inferences from the facts established by the proof, and to choose between conflicting inferences. *Helvering* v. *Lazarus & Co.*, No. 56, this Term; *Helvering* v. *National Grocery Co.*, 304 U. S. 282; *Elmhurst Cemetery Co.* v. *Commissioner*, 300 U. S. 37. The findings of fact by the Board, in our opinion, are supported by overwhelming evidence. But were the evidence less clear, the opinion of the majority of the court below would still be erroneous. The court below concluded that the evidence produced before the Board "permits two inferences to be drawn" (R. 316). It was plainly the duty of the Board, not that of the court below, to draw one rather than the other inference and to declare the result (Section 1003 (a), *supra*, p. 2). *Helvering* v. *Lazarus & Co.*, No. 56, this Term, p. 2.[17]

[17] The cases cited by the court below (R. 316–317), even if applicable to proceedings before the Board of Tax Appeals, are concerned with situations in which, contrary to that here, the evidence leaves the issue completely in the field of conjecture and speculation.

CONCLUSION

The judgment of the court below should be reversed, with direction to dismiss the respondent's petition for review or to affirm the decision of the Board.

Respectfully submitted.

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